



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Release Number: **201149044**
Release Date: 12/9/2011
Date: September 12, 2011
UIL Code: 501.32-00
501.03-05
501.33-00
509.02-02

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear

This is our final determination that you do not qualify for exemption from federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

Since you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, you should follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

In accordance with Code section 6104(c), we will notify the appropriate State officials of our determination by sending them a copy of this final letter and the proposed adverse letter. You should contact your State officials if you have any questions about how this determination may affect your State responsibilities and requirements.

Letter 4038(CG) (11-2005)
Catalog Number 47632S

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at 1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Lois Lerner
Director, Exempt Organizations

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



**DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224**

**TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION**

Date: July 22, 2011

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

LEGEND:

B = Board Member
E = Name of Supported Organization
N = Name of LLC
O = Location
P = City
Q = Date
R = Name of LLC
S = Date
b dollars = \$ amount
c dollars = \$ amount
d dollars = \$ amount
e dollars = \$ amount
f dollars = \$ amount
g dollars = \$ amount
h dollars = \$ amount
j dollars = \$ amount
k dollars = \$ amount
m dollars = \$ amount
n dollars = \$ amount
o dollars = \$ amount
p dollars = \$ amount
q dollars = \$ amount

UIL:

501.32-00
501-03-05
501.33-00
509-02-02

Dear

We have considered your application for recognition of exemption from federal income tax under Internal Revenue Code section 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under section 501(c)(3) of the Code. The basis for our conclusion is set forth below.

Letter 4036 (CG) (11-2005)

ISSUES

1. Do you qualify for exemption under section 501(c)(3) of the Code? No, for the reasons stated below.
2. If you are exempt, are you a supporting organization described in section 509(a)(3)? No, for the reasons stated below.

FACTS

You submitted Form 1023, Application for Exemption Under Section 501(c)(3) of the Internal Revenue Code on S. Information submitted with your application indicates that you were incorporated in O on Q.

You are requesting tax exemption as a Type III functionally integrated supporting organization described in section 509(a)(3) of the Code. Schedule D of your application states you will be "operated in connection with" one or more supported organizations described in section 509(a)(1) or 509(a)(2) and lists the supported organization as E, a public charter school.

Article 3 of your Articles of Incorporation state in pertinent part, "the Corporation is formed exclusively for charitable, scientific, educational, and literary purposes within the meaning of Section 501(c)(3) of the Internal Revenue Code of 1986, as the same may be amended or modified or replaced by any future United States internal revenue law (the "Code"), including without limitation, distributing funds to organizations that qualify as exempt organizations under section 501(c)(3) of the Code, or the corresponding section of any future federal tax code. The specific objectives of the Corporation shall be to support [E], provided [E] is a governmental entity or an organization described in Section 501(c)(3) of the Code, by, but not in limitation of the following:

1. helping [E] secure sources of financing including funding from New Market Tax Credits (NMTC) financing:
2. fundraising and holding endowments on behalf of [E]:
3. making or holding loans to for-profit landlords that charges below market lease rates to [E]:
4. supporting [E] in any other allowable manner."

Article 3 also stated, "The corporation is intended to be a Type III supporting organization operated for the benefit of, but not functionally integrated with, [E] within the meaning of section 509(a)(3)(iii) and 509(f) of the Code and the Treasury Regulations thereunder. In connection with its status as a Type III supporting organization that is not functionally integrated with [E], the corporation intends to distribute annually, to and for the use of E, an amount equal to at

least five percent (5%) of the aggregate fair market value of its assets to the extent such distribution is required by the Code. "

We requested that you amend the purpose clause of your Articles of Incorporation to state that you were formed exclusively for E. You stated that you are in the process of amending the purpose clause and a certified copy will be forwarded under a separate cover. To date, the Amended Articles of Incorporation have not been received.

Article 10 of your Articles of Incorporation provided the number of directors constituting the initial Board of Directors was three and they will serve as the directors until the first annual meeting or until their successors are elected. The names and addresses of the initial board members were specified in the Articles of Incorporation. Your application lists four board members, the three initial board members and B.

Article 2 of your Bylaws state, "the Corporation's primary purpose is to support [E], and any other organizations as may be supported by the Corporation from time to time (collectively the 'Supported Organizations') pursuant to the Corporation's Articles of Incorporation."

Article 4 Section 1 of your Bylaws state in pertinent part, "The number of directors shall be three, until increased pursuant to the following provisions, but shall never be less than three. [E] shall have the sole exclusive authority and discretion to appoint, remove and reappoint one person as one of the directors of the Corporation's Board of Directors. [B] shall serve as the initial [E] director, although not appointed by [E] and shall be subject to confirmation or replacement when [E] has its first opportunity to appoint the initial [E] appointed director. The directors other than the [E] appointed director, shall be elected at the annual meeting of the Board of Directors, and each director elected shall hold office until the next succeeding annual meeting or until his or her successor is elected and shall qualify."

You amended your Bylaws to state your primary purpose is to exclusively support E and E has the sole exclusive authority and discretion to appoint, remove, and reappoint one person as one of the directors of the Corporation's Board of Directors. However, the amendment was not signed by any of the board members.

In addition to the purposes described in Article 3 of the Articles of Incorporation, you will also assist E in securing New Market Tax Credit financing to help E refinance the acquisition, construction, and equipping of its new school located in P. This will include serving as a nonmember manager of a joint venture between E and a so-called New Market Tax Credit "community development entity."

You stated New Market Tax Credits can only be claimed by for profit entities that invest in qualified "community development entities" (CDE's) and then only if the CDE's make investments, and loans to eligible "qualified low-income community businesses" (QALICB's).

You stated you informed E by letter that you incorporated in O and are established as a "supporting organization" to E. You offered to act as Manager of N.

You entered into an Operating Agreement as a non-member Manager with E as the regular member and R as the investor member to form N. You are the non-member Manager of N, which is a Limited Liability Company, treated as a partnership between E and a for profit investor/lender. E is the regular member of N and has a 65.1% interest. R is the investor member and holds 34.9% interest. N receives both an equity investment and loan from a CDE at terms better than standard in the market. Section 1.3 of the Operating Agreement provides that N will manage qualified low income community investment loans (QLICI), lease the QALICB premise, and manage the financing of N. No provision in the Operating Agreement requires N to make any charitable contribution to you, E, or any other charitable organization.

You initially stated you will assist E by fundraising and holding endowments on behalf of E, making or holding loans to landlords that charge below market lease rate to E, and supporting E in any other allowable manner. You later dropped the proposed activity of making or holding loans to landlords that charge below market lease rates to E.

E is the maker of a Promissory Note for b dollars and the payee is N. R is the maker of a Promissory Note for c dollars and the payee is N. You initially stated you will receive d dollars in , e dollars in , and f dollars in in accrued interest. When we asked you to describe the notes and loans you will receive you stated that the figures are in error.

As the Manager of N, you are formed to benefit both E and R. The initial capital contribution by E was g dollars and the initial capital contribution by R was h dollars. Your Operating Agreement does not specify the type of assets contributed by each member. Schedule D of the Operating Agreement shows projected cash distributions of p dollars for each of the first six years and j dollars in year seven for R. E is to receive a cash distribution of k dollars in year seven. There were no contributions shown for the last three years.

Section 4.1 of the Operating Agreement describes the cash allocations and distributions. The first distribution is to be made to R. R is also the first to receive distributions of Capital Proceeds.

Articles 5A of the Operating Agreement states that the Manager has the right, whether or not directed by the investor member to cause N to make a charitable contribution to an operating business, foundation, or another nonprofit of any company property, including cash or a portion of any interest in real property owned by N. However, one of the stipulations is that the cash flow after all charitable contributions of cash is at least sufficient to pay expenses and make distributions required under section 4.1 of the Agreement.

Section 5.6 of the Operating Agreement states, "the Manager may engage in or possess interest in other business ventures of every kind and description for its own account, including without limitation serving as general partner or managing member of other partnerships or limited liability companies, respectively, that own, either directly or through interest in other partnerships or limited liability companies."

The Operating Agreement provided in pertinent part, the purpose of N is to (a) negotiate and enter into the QLICB Loan, (b) lease the QALICB Premises to Operating Business pursuant to

the Site Lease, (c) sublease the QALICB Premises to Operating Business pursuant to the Facility Lease, (d) pay Transaction Cost, (e) deposit the QALICB Working Capital Cash Reserves in QALICB Working Capital Cash Reserve Investment Contract, (f) take any and all other actions necessary or appropriate to further the purposes of the N within the scope of this Agreement, and (g) pursue the above purposes in a manner consistent with the tax exempt status of you, as Manager, and E under Code Section 501(c)(3). In the event of a conflict between you, as Manager, and E's charitable purpose and profit motive of N, the charitable purpose shall take precedence. The foregoing notwithstanding, although it is contemplated that N shall make certain charitable contributions, neither N, you as Manager, nor any Member is required to make any charitable contribution (or a pledge of any charitable contribution) to the you, E or any charitable organization.

N will own real estate that is leased by N to E and used as a traditional school building for its academic programs. You will carry out all of the day-to-day management duties as Manager of N, and, if certain conditions are met, you are authorized to cause N to make donations of net operating income to you to support additional academic programs.

Your initial financial data showed q dollars in revenue for the first three years. This included m dollars in accrued interest on loans/notes receivable and n dollars in Guaranty Fee Income. The total expenses for that same period were o dollars in professional fees. You later submitted revised budgets showing n dollars in gross receipts for , , and . The only expenses were for professional fees equal to the gross receipts. Your financial data did not show any contributions paid to E. You subsequently indicated you do not know how much revenue you will receive because you are a start up entity. However, you state the annual income for E is approximately \$ million dollars.

Your initial Schedule D of your application indicated that you will conduct activities that would otherwise be carried out by E. This contradicts with your statement requesting to be a non-functionally integrated supporting organization. When clarified, you submitted a revised Schedule D indicating you will not conduct activities that would otherwise be carried out by E and you will not distribute 85% of your annual income to E but your narrative description states that you will give 85% of your income to E. As previously stated, your financial data reflects no contributions paid to E.

ISSUE 1 - SECTION 501(c)(3)

Law

Section 501(c)(3) of the Code provides, in part, for the exemption from federal income tax organizations organized and operated exclusively for charitable, religious or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(a)(1) of the Regulations states, in order to qualify under section 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more

exempt purposes. If an organization fails to meet either the organizational or operational test, it is not exempt.

Section 1.501(c)(3)-1(a)(2) of the Regulations states the term "exempt purpose or purposes" means any purpose or purposes specified in section 501(c)(3) of the Code.

Section 1.501(c)(3)-1(c)(1) of the Regulations states that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

In Revenue Ruling 58-547, 1958-2C.B. 275, the Service rules that a lease, to which the parties are both exempt from tax under section 501(c)(3) of the Code and which constitutes a business lease within the meaning of section 514 of the Code, will not be considered substantially related to the charitable, educational, etc. purposes of the lessor solely because the lessor is likewise an exempt organization.

Section 4.03 of Revenue Procedure 2010-9, reads in part as follows:

Exempt status will be recognized in advance of operations if proposed operations can be described in sufficient detail to permit a conclusion that the organization will clearly meet the particular requirements of the section under which exemption is claimed.

(1) A mere restatement of purposes or a statement that proposed activities will be in furtherance of such purposes will not satisfy this requirement.

(2) The organization must fully describe the activities in which it expects to engage, including the standards, criteria, procedures, or other means adopted or planned for carrying out the activities; the anticipated sources of receipts; and the nature of contemplated expenditures.

(3) Where the organization cannot demonstrate to the satisfaction of the Service that it qualifies for exemption pursuant to the section of the Internal Revenue Code under which exemption is claimed, the service will generally issue a proposed adverse determination letter or ruling.

In Better Business Bureau v. United States, 326 U. S. 279 (1945), the Supreme Court stated that the presence of a single nonexempt purpose, if substantial in nature, will preclude exemption under section 501(c)(3) of the Code, regardless of the number of importance of statutorily exempt purposes. Thus the operational standard prohibiting a substantial nonexempt purpose is broad enough to include inurement, private benefit, and operations that further nonprofit goals outside the scope of section 501(c)(3).

In The Schoger Foundation v. Commissioner of Internal Revenue Service, 76 T.C. 380 (1981), the court held if one of the purposes of an organization's activities is substantial and non-

exempt (e.g. commercial), the organization will be denied exempt status under section 501(c)(3), even if the activity also furthers an exempt purpose.

In Plumstead Theatre Society, Inc v. Commissioner, 675 F 2nd 244 (9th Cir. 1982), the Ninth Circuit Court of Appeals affirmed a decision by the Tax Court holding that a 501(c)(3) arts organization's participation in a partnership with for-profit partners would not disqualify it from tax exemption merely because some investors made a profit from the production of a play. The Court found that participation by the investors was necessary for the organization to achieve its exempt purpose. The Court also found particularly relevant: (1) the investors were not shareholders in or officers or directors of the organization; and (2) the agreement gave full control over the operations to the organization and not to the investors.

In Salvation Navy v. Commissioner, T.C.M. 2002-275(2002), the court found that one of the reasons why the organization did not qualify for exemption from federal income tax was because it could not prove that its net earning would not inure to the benefit of a private individual.

Application of Law

Section 501(c)(3) of the Code and Section 1.501(c)(3)-1(a) of the Regulations sets forth two main tests for qualifications for exempt status. An organization must be organized and operated exclusively for purposes describe in section 501(c)(3) of the Code. You pass the organizational test because your Articles of Incorporation state that you are formed for purposes described in section 501(c)(3) and that upon dissolution all assets will go to organizations that are exempt under section 501(c)(3) of the Code.

You must, however, satisfy the operational test. The key requirement is that an organization be operated exclusively for one or more purposes described in section 501(c)(3) of the Code. The facts submitted show that the activities you conduct are not activities described in section 501(c)(3) of the Code.

Section 1.501(c)(3)-1(c)(2) of the Regulations clarifies that an organization is not operated exclusively for exempt purposes if its net earnings inure to the benefit of private individuals. Based on the information you submitted, R, the investor member, will benefit equally as much if not more than E.

Managing a Limited Liability Company in which one of the members is a tax exempt organization under section 501(c)(3) of the Code does not constitute a tax exempt activity simply because both parties are tax exempt. See Revenue Ruling 58-547 and Revenue Procedure 2010-9.

Not only are you the Manager of a Limited Liability Company, but Section 5.6 of the Operating Agreement allows you, the Manager, to engage in or possess interest in other business interests of every kind including serving as the general partner in a partnership or Limited Liability Company, and to make charitable distributions but only after expenses and distributions are made to R, the investor member.

You entered into an Operating Agreement as a non-member Manager with E and R to form N. You have not demonstrated that you have a charitable or educational purpose. As stated in Section 1.3 of the Operating Agreement you will manage QLICI loans, lease the QALICB premise, and manage the financing of N. N is not required to make any charitable contribution to you, E, or any other charitable organization.

Your purpose is to manage N, a Limited Liability Company. N's purpose is to negotiate and enter into a QLICI loan and lease and sublease the QALICB premises. Similar to the organization described in The Schoger Foundation v. Commissioner, supra, you do not satisfy the "not more than an insubstantial part of its activities" standard of section 1.501(c)(3) -1(c)(1) of the Regulations. You have a non-charitable purpose that is substantial in nature. See Better Business Bureau v. United States, supra.

Unlike Plumstead Theatre Society v. Commissioner, supra, the court also found particularly relevant: (1) the investors were not shareholders in or officers or directors of the organization; (2) the agreement gave full control over the operations to the organization and not to the investors. Unlike Plumstead Theatre Society, supra, R, the investor member, has a significant voice in how N is operated.

Furthermore, your letter to E appears that of an arrangement with E as a business deal rather than an agreement between two nonprofit corporations. Once you informed E that you were incorporated as a nonprofit, you and E entered into the "Operating Agreement" along with R, the investor member. Similar to Salvation Navy v. Commissioner, supra, you have not supplied enough evidence to show that R will not benefit significantly from the activities you conduct.

DETERMINATION – ISSUE 1

Based on the information provided on your Form 1023 and supporting documentation, we have concluded that you are not operated exclusively for purposes described in section 501(c)(3) of the Code. You have not shown that your activities are exclusively for purposes described in section 501(c)(3) of the Code. You are formed for the purpose of managing a Limited Liability Company. Therefore, you do not qualify for exemption under section 501(c)(3) of the Code, because you are not operated exclusively for 501(c)(3) purposes.

ISSUE 2 - SECTION 509(a)(3)**Introduction**

We have also considered your application for supporting organization status (non-private foundation status) under section 509(a)(3) of the Code in the event that you would qualify for exemption under section 501(c)(3) of the Code. Our conclusion regarding your private foundation classification under section 509(a)(3) is based on a number of factors discussed in the following materials.

Section 509(a)(3) of the Code provides the term "private foundation" does not include an organization which:

(A) is organized, and at all times thereafter is operated, exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more specified organizations described in section 509(a)(1) or (2),

(B) is operated, supervised, or controlled by or in connection with one or more organizations described in section 509(a)(1) or (2), and

(C) is not controlled directly or indirectly by one or more disqualified persons (as defined in section 4946) other than foundation managers and other than one or more organizations described in section 509(a)(1) or (2).

Section 509(a)(3)(A), in effect, describes as a public charity, an organization which is organized and at all times thereafter is operated, exclusively for the benefit of, to perform the functions of, or carry out the purposes of one or more specified organizations described in sections 509(a)(1) or 509(a)(2). In our discussion of these issues, we are cognizant of the fact that at, all times, you are asserting qualification under section 509(a)(3) under the "operated in connection with" relationship provided in section 1.509(a)-4(i) of the Regulations.

For an organization to qualify as a supporting organization it must pass the organizational and operational test (509(a)(3) (A)), relationship test (509(a)(3)(B)) and a control test (509(a)(3)(C)). You do not pass the operational test and relationship test.

Operational Test

Section 509(a)(3)(A) of the Code provides that, in order to qualify under section 509(a)(3), an organization at all times thereafter is operated, exclusively for the benefit of, to perform the functions of, or to carry out the purposes of one or more specified organizations described in section 509(a)(1) or (2).

Reg. 1.509(a)-4(b)(1) provides that in order to qualify as a supporting organization, an organization must be both organized and operated exclusively "for the benefit of, to perform the functions of, or to carry out the purposes of" one of more specified publicly supported

organizations. If it fails to meet either the organizational test or operational test, it cannot qualify as a supporting organization.

Reg. 1.509(a)-4(e)(1) provides that a supported organization will be regarded as "operated exclusively" to support one or more specified public supported organization only if it engages solely in activities which support or benefit the specified publicly supported organizations.

Application of Operational Test

You are not operated exclusively for the benefit of specified publicly supported organizations as required by section 509(3)(a)(A). The only activity that you are conducting is managing N, a Limited Liability Company. You have not demonstrated that you will provide any income to E and you are not conducting any activities on behalf of E. Furthermore, you are also formed to benefit R. You have not demonstrated that you are operated exclusively to support E, the publically supported organization as required in Section 1.509(a)-4(e)(1) of the Regulations.

Relationship Test

Reg. 1.509(a)-4(i)(1)(i) provides that generally a supporting organization will be considered as being "operated in connection with" one or more publicly supported organizations only if it meets the "responsiveness test" and the "integral part test." This relationship rest upon the finding that the supporting organization is responsive to the needs or demands of the supported organizations and maintains an integral part or significant involvement in the supported organizations affairs. You do not meet the responsiveness test or the integral part test.

Responsiveness Test

Reg. 1.509(a)-4(i)(2)(i) provides that a supporting organization will meet the "responsiveness test" if the organization is responsive to the needs or demands of the publicly supported organizations.

See Section 1.509-4(i)(2)(ii) of the Regs. states an organization will pass the responsiveness test if;

- a. one or more officers, directors, or trustees of the supporting organization are elected or appointed by the board members of the supported organization, or;
- b. one or more board members of the governing body of the supported organization are also officers, directors, or trustees of, or hold other important officers in the supporting organization, or;
- c. the supporting organization's officers, directors, or trustees maintain a close and continuous working relationship with the officers, directors, or trustees of the supported organization.

Once the relationship has been established, the supporting organization must demonstrate that because of the relationship, the officers, directors, or trustees of the publicly supported

organization have a significant voice in the investment policies of the supporting organization; the timing of grants; the manner of making grants; and otherwise directing the use of the supporting organization's income or assets.

Application of Responsiveness Test

You do not meet the responsiveness test because none of your officers are appointed by the specified supported organization. Your initial Bylaws stated, "The number of directors shall be three, until increased pursuant to the following provisions, but shall never be less than three. E shall have the sole exclusive authority and discretion to appoint, remove and reappoint one person as one of the directors of the Corporation's Board of Directors. B shall serve as the initial E director, although not appointed by E and shall be subject to confirmation or replacement when E has it first opportunity to appoint the initial E appointed director."

We requested that you amend your Bylaws to state that E will appoint the E director. We did receive the amendment to your Bylaws but it was not signed by any of your officers. You did not submit any documentation that E would have a significant voice in the use of the income or assets. Furthermore, your Bylaws state that the board members who are not E appointed members will be selected by the Board of Directors.

Your Bylaws and Articles of Incorporation state that there will be three board members. However, your application lists four members, the initial three board members and B. You do not meet the responsiveness test.

Integral Part Test

Reg. 1.509(a)-4(i)(3)(i) provides that a supporting organization will be considered to meet the "integral part test" if it maintains a significant involvement in the operations of one or more publicly supported organizations and such publicly supported organizations are in turn dependent upon the supporting organization for the type of support which it provides. A supporting organization may satisfy the "integral part test" by meeting either the "functional support" test, also known as the "but-for" test, or the "attentiveness" test.

Reg. 1.509(a)-4(i)(3)(ii) provides that a supporting organization will meet the "functional support" test if the activities engaged in for or on behalf of the publicly supported organizations are activities to perform the functions of, or to carry out the purposes of, such organizations, and, but for the involvement of the supporting organization, would normally be engaged in by the publicly supported organizations themselves.

Reg. 1.509(a)-4(i)(3)(iii)(a) provides that a supporting organization will meet the "attentiveness" test if the supporting organization makes payments of substantially all of its income to or for the use of one or more publicly supported organizations, and the amount of support received by one or more of such publicly supported organizations is sufficient to insure the attentiveness of such organizations to the operations of the supporting organization. In addition, a substantial amount of the total support of the supporting organization must go to those publicly supported organizations, which meet the attentiveness requirement of this subdivision with respect to such

supporting organization. Generally, the amount of support received by a publicly supported organization must represent a sufficient part of the organization's total support so as to insure such attentiveness. However, if such supporting organization makes payments to, or for the use of, a particular department or school of a university, hospital or church, the total support of the department or school shall be substituted for the total support of the beneficiary organization.

Section 1243 of the Pension Protection Act (PPA) effectively added section 4943(f)(5) to the Code. This section defines a functionally integrated Type III supporting organization and a non-functionally integrated Type III supporting organization. A functionally integrated supporting organization is one that is not required to make payments to supported organizations due to the fact that the activities of the organization are related to directly performing the functions of, or carrying out the purposes of, the supported organization. A non-functionally integrated supporting organization is one that makes payments to the supported organizations.

Application of Integral Part Test

You provided conflicting information if you are a non-functionally integrated or functionally integrated Type III supporting organization. Based on the information that was submitted, you do not qualify as a non-functionally integrated or a functionally integrated Type III supporting organization.

You do not meet the requirements for a non-functionally integrated supporting organization because you do not meet the payout requirement. Thus far, you have not distributed any funds to E and you have no immediate plans to do so. The revised financial data that you submitted shows total income of n dollars and professional expenses for the same amount. Even if you were to contribute all n dollars to E this would not be enough to warrant their attentiveness since the annual income for E is approximately \$8 million dollars. Thus, the amount contributed to E is not sufficient to warrant E's attentiveness. Therefore, you do not meet the attentiveness testing in order to satisfy the integral part test.

You do not meet the requirements for a functionally integrated supporting organization because you are not conducting an activity that is normally conducted by the supported organization. Your only activity is managing N. This is not an activity that is normally carried on by the supported organization. Therefore, you do not meet the "but for" test in order to satisfy the integral part test.

Conclusion

Based on the facts you have failed to meet the relationship test of Section 509(a)(3)(B) of the Code. You have failed to demonstrate that you will maintain a significant involvement in the operations of the publicly supported organization as described in Section 1.509(a)-4(i)(3)(i) of the Regulations.

Control Test

Section 509(a)(3)(C) of the Code, in effect, provides that public charity status under section 509(a)(3) is precluded for an organization that is controlled directly or indirectly by one or more disqualified persons (as defined in section 4946) other than foundation managers and other than one or more organizations described in paragraph (1) and (2).

Section 4946(a) of the Code defines a disqualified person as a substantial contributor to the foundation. Section 4946(a)(1)(C) includes in its definition of a substantial contributor an owner of more than 20%, (i) the total combined voting power of a corporation, (ii) the profits interest in a partnership, or (iii) the beneficial interest of a trust or unincorporated enterprise which is a substantial contributor to the Foundation.

Section 1.509(a)-4(j)(1) of the Regulations provides that if a person who is a disqualified person with respect to a supporting organization, such as a substantial contributor to the supporting organization, is appointed or designated as a foundation manager of the supporting organization by a publicly supported beneficiary organization to serve as the representative of such publicly supported organization, then for purposes of this paragraph, such person will be regarded as a disqualified person rather than as a representative of the publicly supported organization.

An organization will be considered "controlled," for purposes of section 509(a)(3), if the disqualified persons, by aggregating their votes or positions of authority, may require such organization to perform any act which significantly affects its operations or may prevent such organization from performing such act. This includes, but is not limited to, the right of a substantial contributor or his spouse to designate annually the recipients, from among the publicly supported organizations of the income attributable to his contribution to the supporting organization.

Application of Control Test

You are not controlled directly or indirectly by one or more disqualified persons. You meet the control test.

DETERMINATION - ISSUE 2

Based on our analysis of your actual and proposed activities, you have failed the operational test and the relationship test. As a result of our analysis, and in light of the applicable law, we have determined you do not qualify for exclusion from private foundation status under section 509(a) (3) of the Code.

CONCLUSION

In conclusion, we have determined you do not qualify for tax exemption as an organization described in section 501(c)(3) of the Code. Even if we determined that you were described in section 501(c)(3), you would be a private foundation and not a supporting organization under section 509(a)(3) of the Code.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination. If your statement does not provide a basis to reconsider our determination, we will forward your case to our Appeals Office. You can find more information about the role of the Appeals Office in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*.

Types of information that should be included in your appeal can be found on page 2 of Publication 892. The statement of facts (item 4) must be accompanied by the following declaration:

"Under penalties of perjury, I declare that I have examined the statement of facts presented in this appeal and in any accompanying schedules and statements and, to the best of my knowledge and belief, they are true, correct, and complete."

The declaration must be signed by an officer or trustee of the organization who has personal knowledge of the facts.

Your appeal will be considered incomplete without this statement.

If an organization's representative submits the appeal, a substitute declaration must be included stating that the representative prepared the appeal and accompanying documents; and whether the representative knows personally that the statements of facts contained in the appeal and accompanying documents are true and correct.

An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you during the appeal process. If you want representation during the appeal process, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. You can find more information about representation in Publication 947, *Practice Before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to appeal as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848, and any supporting documents to the applicable address:

Mail to:

Internal Revenue Service
EO Determinations Quality Assurance
Room 7-008
P.O. Box 2508
Cincinnati, OH 45201

Deliver to:

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Room 7-008
Cincinnati, OH 45202

You may fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

We have sent a copy of this letter to your representative as indicated in your power of attorney.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Lois Lerner

Lois Lerner
Director, Exempt Organizations

Enclosure, Publication 892